

DEPARTMENT OF TRANSPORTATION

STATEMENT OF

CLYDE J. HART, JR.
MARITIME ADMINISTRATOR

BEFORE THE

COMMERCE, SCIENCE AND TRANSPORTATION COMMITTEE
U.S. SENATE

IN SUPPORT OF FISCAL YEAR 2001 AUTHORIZATION
FOR THE MARITIME ADMINISTRATION

May 16, 2000

Mr. Chairman and Members of the Committee:

I welcome the opportunity to be here today to discuss the Maritime Administration's (MARAD's) Fiscal Year 2001 authorization request. I know that I do not need to tell you that MARAD is committed to U.S. merchant mariners and our maritime industry. The U.S.-flag merchant marine and the domestic maritime industry perform yeoman service for America at an affordable price. They deliver a cornucopia of goods to and from foreign markets. In war or crisis, they have a proven track record of responding professionally, often in dangerous environments, to the critical needs of our U.S. armed forces. America's preeminence in economic and military affairs has been bolstered in no small part by this industry. May 25th marks the 50th anniversary of MARAD as an executive agency. All who have had the privilege to serve here over the years are determined that this year be one that will long be remembered.

Full funding of MARAD's budget request will allow the agency to address high priority needs -- such as the renovation of the Nation's Merchant Marine Academy, as well as fund our ongoing efforts in the Maritime Security Program (MSP), shipbuilding, the Marine Transportation System Initiative, the National Defense Reserve Fleet and Ready Reserve Force, cargo preference, and maritime education and training. The proposal would also provide MARAD with necessary time to develop a plan to dispose of obsolete government vessels. As a former staff counsel on this committee, I recognize the inevitable competing demands for scarce resources. However, we at MARAD strongly believe that every dollar requested is needed. This budget request in the first year of the new century will be viewed as an indication of what the future holds for this industry. Secretary Slater and I have made passage of the MARAD Authorization Act for FY 2001 a priority.

I will now summarize our FY 2001 budget request and note for the committee the contributions and progress of MARAD programs during the past year.

Maritime Security Program

The Maritime Security Act of 1996 established a Maritime Security Program (MSP) with the goal to ensure the continued presence of a fleet of U.S.-flag vessels engaged in international trade, that is also able to meet national security sealift requirements in times of war or national emergency. In FY 2001, we request a total of \$98.7 million for MSP payments. The request represents payments of approximately \$2.1 million each to 47 vessels with proven national security capabilities.

As of January 1, 2000, all of the 47 ships enrolled in MSP were participating in the program according to their operating agreements with MARAD. The MSP continues to be a truly innovative program – at about half the cost per vessel of the Operating-Differential Subsidy program it replaced. MSP operators, through participation in the Voluntary Intermodal Sealift Agreement (VISA) program, make not only each participating vessel, but their state-of-the-art intermodal transportation system, available to the Department of Defense (DOD) for sealift support. This program provides essential support to DOD as the military increasingly relies on the commercial transportation industry for logistics capability. The MSP is a shining example of successful partnering between the Government and the private sector.

Mr. Chairman, as you know, authorization for the MSP ends in FY 2005. During FY 2000, we will conduct an evaluation of the impact of the MSP and VISA programs on MARAD and DOT national security goals of increasing the readiness and the capability of the commercial transportation system to meet national defense needs. This evaluation is being undertaken as part of our commitment to the Government Performance and Results Act.

Shipbuilding

Revitalization of the nation's shipbuilding continues to be an Administration priority. The Maritime Guaranteed Loan, or Title XI, Program is the centerpiece of our shipbuilding revitalization initiative, and has been very successful in stimulating shipbuilding activity. Title XI loan guarantees enable ship owners and U.S. shipyards to borrow private sector funds on more favorable terms than might otherwise be available. Government funds are obligated to offset the credit risk of loan guarantees and for administrative costs. Since 1993, shipyard construction and shipyard modernization projects costing approximately \$6 billion have been approved by MARAD. An authorization request of \$2 million for the cost of loan guarantee commitments would enable MARAD to provide loan guarantees of up to \$40 million based on a 5 % loan subsidy rate. A carryover of amounts previously authorized for loan guarantees into fiscal year 2001 will allow for an appropriate level of loan guarantees. The \$4.179 million request for administrative expenses will enable MARAD to manage both the existing portfolio of loan guarantees and new guarantees.

Thanks to Title XI funding, 11 new state-of-the-art double hull tankers have been delivered from U.S. shipyards since enactment of the shipbuilding revitalization initiative in 1993. These deliveries marked the first time that an ocean-going petroleum tanker had been built in the United States in over a decade, and the first ever deliveries of commercial double hull tankers in this country. Title XI financing has also been instrumental in the construction of numerous double-hull tank barges being utilized on the inland and coastal waterways.

This past year, more advances in modern American shipbuilding have been achieved by the Title XI program. In April of 1999, Secretary Slater announced that two large ocean-going cruise ships will be built in the United States for the American Classic Voyages Company -- the first time in nearly a half century that large, ocean-going cruise ships will be built in an American shipyard. The vessels are designed to embrace the amenities of modern cruise ship luxury, safeguard the environment and will carry up to 1,900 passengers each. This design was a direct result of a MARAD administered project under the now terminated MARITECH program. Construction is scheduled to begin sometime this year. Title XI loan guarantees of more than \$1 billion have helped make this project a reality and, we hope, will help to launch a new segment of the industry. MARAD's Capital Construction Fund (CCF) Program has also made significant contributions to U.S. shipyard activity, such as facilitating the construction of three double-hull tankers for ARCO Marine in Louisiana, and two roll on/roll off (RO/RO) vessels for Saltchuk Resources at NASSCO.

Mr. Chairman, I am aware of your interest in the status of the Quincy Shipyard Project. As you know, in 1995, Massachusetts Heavy Industry, Inc. (MHI) approached MARAD regarding a Title XI loan guarantee to reactivate and modernize the Quincy Shipyard. MARAD determined that MHI would be unable to demonstrate the economic soundness necessary to secure a Title XI loan guarantee. Public Law 104-324, the Coast Guard Authorization Act of 1996, directed the Secretary to waive the Title XI requirements for economic soundness. Pursuant to that authority, on November 1, 1996, MHI received approval for a loan guarantee in the amount of \$55 million to reactivate and modernize the shipyard. As required by the legislation, MARAD protected its security position to the maximum extent possible by obtaining a first mortgage, instituting strict escrow fund disbursement procedures, and entering into a favorable intercreditor agreement.

MHI missed a regularly scheduled \$1.55 million debt service payment on June 1, 1999. Upon its request and the concurrence of the lending institution, Fleet Bank, MARAD deferred the payment until December 1, 1999. However, on December 1, 1999, MHI missed its second consecutive regularly scheduled payment of \$2.1 million on the guaranteed obligations, as well as the payment owed from June 1st.

MARAD and MHI had continuing discussions in an attempt to provide a funding mechanism for the December 1, 1999 payment, at the urging of Fleet Bank. MARAD extended until late February 2000 the date on which this payment could be made to give MHI the fullest opportunity possible to make those payments. However, MHI was unable to obtain the necessary financing -- in a form acceptable to MARAD -- to make this payment or to complete the shipyard without substantially impairing MARAD's security and increasing MARAD's liability under the loan guarantee. Thus, a demand for payment under the Title XI guarantee was made to MARAD by the lending institution. On February 25, 2000, the agency honored this demand by making a payment for \$59.1 million on the defaulted loan, which was the principal amount plus accrued interest. MHI subsequently filed for Chapter 11 bankruptcy protection and MARAD is moving to foreclose on the shipyard.

Mr. Chairman, let me reassure you once again, MARAD has worked closely with the Department's Office of the Inspector General (DOT IG) throughout this project. On September 15, 1999, the DOT

IG recommended that, until it was clear whether the surety would act under its performance bond, MARAD freeze funds contained in the escrow fund established to pay for the reactivation. MARAD subsequently froze the escrow funds and work at the shipyard, which had been halted in August, was never resumed as a result of MHI's contract dispute with its general contractor. These funds, approximately \$12 million, were used to offset MARAD's February 25, 000 payment on the loan guarantee, thereby reducing our initial losses. At all times, MARAD kept members of Congress with an interest apprised of the status of the Quincy Shipyard reactivation and modernization project.

Mr. Chairman and Members of the Committee, it is our goal to see that productive use of the shipyard can someday be achieved. However, there remain both environmental and financial concerns which must be resolved through court proceedings.

The National Defense Reserve Fleet and the Ready Reserve Force

The National Defense Reserve Fleet (NDRF) was established in 1946 in order to meet reserve sealift requirements for national defense purposes. NDRF vessels are located at three major sites: James River, Virginia; Beaumont, Texas; and Suisun Bay, California. There are currently 257 ships in the NDRF, 90 of which comprise the Ready Reserve Force (RRF). RRF ships are maintained in various states of readiness, and can sail in either 4, 5, 10, 20 or 30 days. The majority of RRF ships are outported to various locations throughout the country in proximity with likely loadout ports established by the Department of Defense.

When activated, RRF ships are fully crewed by civilian merchant mariners working to support DOD missions. From the time of the Revolutionary War to the present, the American merchant marine has always played a critical role in the protection of U.S. interests. The tradition continues today. MARAD's RRF ships played a critical role during the Gulf War, and have been used to provide assistance during crises in Somalia, Haiti, Bosnia, and hurricane-ravaged Central America. Four RRF ships are currently deployed as part of DOD's prepositioned forces to respond quickly to regional conflicts throughout the world.

Ship Scrapping

Some NDRF vessels remain idle at Reserve Fleet sites because they are beyond their useful lives. Currently, 112 vessels in the NDRF have been determined to be obsolete and are slated for scrapping. It is estimated that the inventory of obsolete vessels will increase to 134 at the beginning of the year 2001 if additional vessels are not disposed of.

MARAD's primary means of disposing of obsolete vessels has been to sell them for scrapping. Under the National Maritime Heritage Act of 1994, the agency is required to dispose of obsolete vessels in the NDRF by September 30, 2001, in a manner that maximizes financial return to the United States. However, since 1995, MARAD has refrained from scrapping obsolete NDRF vessels overseas due to concerns about the environment and worker health and safety at the foreign scrap sites. Although MARAD has sought to scrap the vessels in the domestic market, where environmental and safety standards are high, the capacity of this market is limited. Moreover, the Department of the Navy,

which is responsible for the disposal of obsolete combatant vessels, has initiated a pilot program to pay for the costs of disposing of its obsolete vessels. MARAD has been reviewing bids and performing increased contract monitoring and oversight. Between 1987 and 1994, 130 vessels were sold to foreign scrappers for \$108/ton, but only 10 vessels were awarded to be scrapped domestically in 1997-98 at an average of \$4.60/ton. Last year, 12 vessels were awarded for only 27 cents per ton and three vessels were sold for \$10 each, to be scrapped domestically. Many of the vessels that were sold domestically have not been picked up by the buyers. One sales agreement for five vessels was terminated last year because the purchaser did not take possession of the vessels.

MARAD will be unable to dispose of all of the obsolete vessels in the NDRF by the September 30, 2001 deadline. Therefore, this year's authorization bill proposes to extend the disposal date by five years to September 30, 2006. This extension will provide MARAD with additional time to develop an action plan and begin implementation of the plan to dispose of this growing number of vessels, given current scrapping conditions. The objective we all work to accomplish is to scrap vessels in an environmentally sound and economically reasonable manner.

I am sure that you are aware that about 40 NDRF vessels -- containing PCB's (polychlorinated biphenyls), asbestos, fuel oil and other hazardous substances -- are in extremely poor condition. These ships are monitored closely by MARAD to prevent sinking or a hazardous discharge. Nevertheless, they continue to deteriorate. To date, the Department of Defense has provided the necessary resources to ensure that no environmental damage occurs.

Cargo Preference

U.S. cargo preference laws are an important part of the overall statutory program to support the privately owned and operated U.S.-flag merchant marine. These laws require that a certain percentage of Government-impelled cargo be carried on U.S.-flag vessels. By guaranteeing the availability of cargo to U.S.-flag ships, these laws are important to the financial viability of U.S.-flag vessel operating companies. The laws ensure that the vessels, trained crews, and vessel service industries continue to be available to support our Nation's economic and national security. The laws also help protect our ocean commerce from domination by foreign companies, many of which enjoy significant tax breaks and direct subsidies. Monitoring compliance with the U.S. cargo preference laws is essential in encouraging other Federal agencies to maximize the use of U.S.-flag vessels. MARAD provides an annual report to Congress on the level of compliance among other Federal agencies, and is currently updating its cargo preference regulations.

This year's authorization proposal contains a provision that was also contained in our Fiscal Year 2000 proposal, to establish a one-year waiver of the "three year rule" which mandates that foreign-built vessels brought under the U.S. flag must wait three years before carrying food aid preference cargoes. The proposed amendment provides a limited opportunity for modern, foreign-built bulk and break bulk vessels to register under the U.S.-flag and be immediately eligible to carry preference cargo in international trade. In return, the vessels must have any additional shipyard work necessary to become U.S.-flagged performed in the United States. The vessels would not be granted pre-approval to leave U.S. registry under section 9(e) of the Shipping Act, 1916, or be entitled to any benefit of the Capital Construction Fund, under section 607 of the 1936 Act.

We expect food aid programs for Russia, North Korea, and the Administration's recently announced Section 416(b) program, to generate about 5.2 million metric tons of bulk grain shipments this year, including the normal flow of aid cargoes to other countries. The existing U.S.-flag drybulk capacity may not be able to meet the anticipated need. The waiver would help to ensure that there are enough U.S.-flag vessels to carry 75 percent of the food aid to these countries, as required by law.

Most importantly, this amendment could improve the vessel profile of the U.S.-flag drybulk and breakbulk fleets, add jobs for U.S. merchant mariners capable of crewing sealift ships in a mobilization, and increase the percentage of U.S. foreign commerce carried in U.S.-flag vessels. Additional modern vessels in the U.S.-flag fleet also would increase the competition for carriage of government-impelled cargoes. This could result in substantial cost savings to the U.S. Government. Because these vessels would only be eligible for foreign trade, this proposal has no impact on the Administration's firm commitment to the U. S.-build requirement of the Jones Act. Foreign-built vessels have always been eligible to carry preference cargo after being registered for three years as a U.S.-flag vessel.

We also propose changing the cargo preference year for determining compliance so that it coincides with the Federal Government fiscal year. This would simplify record keeping and management of the program without impact on any involved agencies or shippers. Parties affected by the change have expressed support for the change.

Maritime Education and Training

A significant portion of MARAD's budget request is intended for ongoing maritime education and training activities. Our request for operations and training funds includes approximately \$37.2 million to operate the United States Merchant Marine Academy at Kings Point, New York. The Merchant Marine Academy offers a four-year undergraduate program that leads to a Bachelor of Science Degree, and a merchant marine license as a Third Mate or Third Assistant Engineer, or a dual license. In addition, the students are enrolled as midshipmen and are commissioned upon graduation as Ensigns in the U.S. Naval Reserve. The Academy's significance as a world-renowned institution of maritime education cannot be overestimated. Not only does the Academy produce highly qualified officers for the merchant marine, but it is also the largest single source of inactive duty Naval Reserve Officers. In peacetime, Academy graduates create and operate efficient, cost-effective marine transportation systems. In times of conflict, Academy graduates crew the ships that support our troops.

This year's funding request of about \$37.2 million for the Academy includes a \$3.3 million increase over funds appropriated in FY 2000, including mandatory Federal salary and related cost increases. The increase will fund both operational and capital improvements at the Academy. The increase for operational improvements, approximately \$1 million, will enable the Academy to improve existing academic and administrative programs, the costs of which have escalated due to contractual manpower and equipment/supplies cost increases. The remainder of the program increase requested is designated

for capital improvements to address a serious maintenance backlog at the Academy's facilities. Because the condition of the utility systems in Academy buildings affects the health and safety of the students, faculty and staff, these repairs are a priority. An overall facilities master plan is under development at the Academy, and is expected to be completed in July.

In addition to the funding for the Merchant Marine Academy, approximately \$9.5 million is requested for financial assistance to the six State maritime academies. The State academies, like the Merchant Marine Academy, offer training for qualified individuals to become officers in the U.S. merchant marine. A portion of the requested funding will support the Student Incentive Payment (SIP) Program at the state academies, which results in a service obligation to the maritime industry and the Armed Forces reserves for the recipients. The request will also fund the costs of maintenance and repair for MARAD ships on loan to the State academies as training ships. Approximately \$2.5 million is needed to renovate the New York Maritime Academy's aging training ship, the EMPIRE STATE.

Marine Transportation System Initiative

Today, over two billion tons of goods produced or consumed in the United States move through our Nation's ports and waterways. This volume is expected to more than double over the next 20 years. The number of recreational users is also expected to grow by over 65 percent to more than 130 million annually in the next 20 years, and high-speed ferry transportation is experiencing rapid growth in response to land-transport congestion. Cruise ships anticipate attracting 6.5 million passengers by the year 2002. Military reliance on the Marine Transportation System (MTS) for force projection and sustainment is also expected to grow in the new millenium.

Congress recognized the importance of the Marine Transportation System (MTS) when, as part of the Coast Guard Authorization Act of 1998, it tasked the Secretary -- through MARAD and the Coast Guard -- to establish a task force to assess the adequacy of the nation's MTS to operate in a safe, effective, secure and environmentally sound manner. The MTS initiative was launched by Secretary Slater nearly two years ago. Last September, the Secretary released a report to Congress entitled *An Assessment of the U.S. Marine Transportation System*, representing an intense joint effort by industry and Government. Secretary Slater has made it clear that the report will serve as the "blueprint" for the future of our MTS. On January 13, 2000, MARAD announced the establishment of the Marine Transportation System National Advisory Council (MTSNAC). The charter for the Council became effective January 28, 2000. The MTSNAC will advise the Secretary of Transportation, through MARAD, on current and future matters relating to the MTS --waterways, ports, and their intermodal connections. The MTSNAC will address: strategies to ensure a safe, environmentally sound, and secure MTS that improves the global competitiveness and national security of the United States; issues and concerns raised by the marine transportation industry; and other matters at the Secretary's request.

The Council will be composed of representatives from approximately 31 non-Federal organizations, representing a cross section of the diverse components that comprise the MTS, including private sector organizations and state

and local public entities. The individual non-federal participants have been nominated by their organizations. The first Council meeting will take place next week on May 24th.

MARAD welcomes its continued leadership in this initiative, and we take our responsibility very seriously. We look forward to continuing our partnership with the U.S. Coast Guard and others involved in this important effort. America's marine transportation system has always delivered the goods and we intend to help make sure that this tradition continues.

Manpower Needs

Among the ongoing efforts at MARAD is the assessment of the supply of mariners to meet commercial and mobilization crewing requirements, now and in the future. Right now, MARAD is seeing and hearing of recruitment and retention problems in the seagoing workforce, just as every industry is facing labor shortages in this vibrant economy. Based on our analysis of mariner data, there are enough qualified active seafarers to crew the DOD organic fleet for a short duration, but this could dry up much of the pool. An extended mobilization of the entire government-owned surge fleet would create pressure to rotate government and commercial ship crews, by augmenting the pool with inactive mariners. There is likely to be a mismatch between available mariners and the specific skills needed to fully activate the DOD organic fleet. We are also concerned that shoreside commitments of some of the inactive mariners – such as work and family -- may keep them from volunteering to serve, even with re-employment rights. These uncertainties concern us.

American Fisheries Act

The American Fisheries Act of 1998 (PL 105-277) assigned MARAD the responsibility to ensure that proper citizenship standards are adhered to for ownership of fishing vessels 100 feet or greater. New regulations will require us to rigorously scrutinize transfers of ownership or control, with particular attention to leases, charters, mortgages, and financing arrangements for fishing vessels.

The final rule to implement the new citizenship requirements of the American Fisheries Act is currently in clearance within the Department of Transportation and will be forwarded to the Office of Management and Budget shortly. Because of the complexity of the issues involved, additional time was required to complete the final rule, which we expect to publish in the *Federal Register* in early June.

Administrative Waivers of the Coastwise Laws for Small Passenger Vessels

Mr. Chairman, I would like to report that one of your own initiatives is now up and running at MARAD – the administrative process for waiver of the U.S.-build requirement contained in the Passenger Vessel Services Act for small vessels, which was part of the Coast Guard Authorization Act of 1998. Under this provision, MARAD is charged with establishing and administering a waiver process that allows vessels carrying less than 12 passengers to engage in coastwise transportation. Waivers are available to qualified vessels so long as the intended employment of the vessel would not harm the domestic boat building industry or the existing business of any domestically built vessel.

Final regulations were published in the *Federal Register* on February 11, 2000. We have received 15 applications to date, and three applications have been approved with many others close to completion. We expect to receive about fifty applications each year. We are pleased to have been selected to administer this program. It offers a fair alternative to small vessel owners who might otherwise be prohibited from employing their vessels in coastwise transportation.

Conclusion

Mr. Chairman, the successes that MARAD can claim to date did not come without help. Committee Members and staff have determined not only the amounts of our authorizations, but also how we conduct business. I noted earlier that the year 2000 represents a special one for us, a year in which we not only wish to celebrate accomplishments but to reach out as never before to industry and Congress. If we are to create the domestic maritime industry that will embody the MTS vision statement in our report to Congress last September, we need your continued support. We at MARAD welcome the responsibilities and challenges that have been given to us and pledge our determination to meet those duties fully as stewards of the public's trust. This concludes my prepared statement. I would be happy to address any questions you may have at this time.

##

